



# UTAH TAX REVIEW COMMISSION

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## **Findings and Recommendations** **Property Taxes and the Financing of Water Development and Delivery**

**As Adopted November 15, 2002**

### Findings

1. In 1995, Utahns used about 5 million acre feet of water, with about 80 percent of this amount devoted to agriculture.
2. Water conservancy district officials<sup>1</sup> and others presented extensive testimony to the Utah Tax Review Commission (TRC) regarding the role of property taxes in financing water development and delivery. These officials testified that:
  - a. Because Utah is an arid state, it must devise ways to capture, divert, and store water from melted snow and prevent this water from running downstream.
  - b. These storage, diversion, transmission, and treatment facilities require capital.
  - c. Property taxes are a component of ensuring access to capital markets. Eliminating the property tax as a source of revenue would increase the cost of capital. It would also possibly jeopardize bond ratings because the investment community regards property taxes as a reliable source of revenue.
  - d. Some districts have entered into repayment contracts for loans obtained from the United States. These contracts require that a certain percentage of repayment come from district assessed property tax revenues.
  - e. Utah has adopted the public policy that development and delivery of water should be a public and not a private enterprise. A pricing system, although efficient, would lead to an inequitable distribution of water.<sup>2</sup>
  - f. A plentiful and reliable water supply is essential to the state's public health, quality of life, and future economic development. Failure to develop an adequate water supply will weaken the overall strength and vitality of the state.
  - g. American farmers are the most efficient food producers in the world. Providing plentiful food at moderate prices raises everyone's standard of living.

3. The TRC received testimony from Mr. B. Dell Gardner, Professor Emeritus, Brigham Young University, regarding the effects of the underpricing of water due to the use of property taxes. He testified that:
  - a. In a free enterprise system, price is a signal both as to how to allocate resources and as a reflection of scarcity. For consumers, price represents the unit cost that determines how much of a commodity will be demanded. For suppliers, price represents the per unit of revenues to the water seller or the amount of the resource that will be supplied by the sellers at different prices.
  - b. In the political arena, there will be pressure to satisfy excess demand by increasing the water supply through a subsidy and that political leaders seek to satisfy the excess demand caused by underpricing water.
  - c. The best way to prevent infeasible water projects is to insist that the beneficiaries, the users, pay the full cost.
  - d. Water planners incorrectly assume that demand for water is price insensitive. Research shows that the true elasticity of demand is somewhere between  $-.5$  and  $-.77$ . This means if the price of water is increased by 10 percent the amount of water demanded will fall by as much as 7.7 percent.
  - e. There are two preferred ways to finance future water development. The first method is through average cost pricing where the cost of developing new water sources is included in the price that everyone pays—both old and new consumers. The second method is more efficient, but is politically difficult. It requires new connections to pay the full cost of developing new water supplies. However, as income and population grows consumers may be willing to spend more on water.
  - f. Under the current financing system, the subsidized water price is capitalized in the value of the land resulting in a net transfer of wealth to owners of agricultural lands.
4. Out of 14 major water conservancy and water improvement districts in Utah, 4 have outstanding general obligation bonds totaling about \$166,705,000.<sup>3</sup> Of this amount, about 89 percent is held by the Central Utah Water Conservancy District.
5. Of these same 14 water districts, 11 have outstanding revenue bonds totaling about \$269,000,000.<sup>4</sup> Some of these districts have pledged to levy property taxes to cover operation and maintenance costs, thereby ensuring an adequate unencumbered revenue stream to repay these revenue bonds.
6. During FY 2001, the five largest wholesale water districts<sup>5</sup> collected about \$46,000,000 in property taxes. Of this amount, almost \$25,000,000 was collected by the Central Utah Water Conservancy District.

## Recommendations

Based on the above findings, the Utah Tax Review Commission (TRC) recommends the following to the Governor and Legislature.

1. Water districts should not levy a property tax to pay for operation and maintenance costs.
2. Recognizing that reliance on property tax revenues by water districts must be gradually reduced over several years, the TRC recommends the following implementation steps:
  - a. Except in extraordinary circumstances, water districts should be discouraged from issuing new general obligation bonds.
  - b. In some revenue bond agreements, water districts have pledged to levy a property tax to pay operation and maintenance costs. This stipulation has been included in both Master Resolutions and Supplemental Resolutions. The TRC recognizes that the Legislature may not impair contracts and that these current agreements must be honored. However, the TRC strongly encourages the Governor and Legislature to find a way to end this practice by water districts when issuing new revenue bonds.
  - c. Any new agreement between a water conservancy district and the United States that obligates that water conservancy district to levy a property tax should be discouraged or closely scrutinized.
  - d. Any property tax that is levied to pay for operation and maintenance costs (with the exceptions as outlined above) should be gradually reduced, and if necessary, replaced with revenue from water charges.
3. The TRC recognizes that some water districts are obligated to levy a property tax either under a repayment contract with the United States or under a general obligation bond agreement.
4. The TRC recognizes that rural and new water conservancy districts operate under unique circumstances and that it may be appropriate, under certain conditions, for these districts to levy a property tax to pay for operation and maintenance costs. It may also be appropriate for these districts to levy a property tax to pay for start-up costs when no state funding is available.

1. The TRC received testimony from the following individuals representing water districts, their financial advisors, and state agencies: Christine Finlinson, Central Utah Water Conservancy District; David Ovard, Jordan Valley Water Conservancy District; Scott J. Robertson, Lewis, Young, Robertson and Burningham; John Crandall, George K. Baum and Company; Randy Crozier, Duchesne Water Conservancy District; Russ Donahue, Rural Water Users Association; Don Ostler, Division of Water Quality; Kevin Brown, Division of Drinking Water; Tage Flint, Weber Basin Water Conservancy District; Ronald Thompson, Washington County Water Conservancy District; and Richard Scott, Chapman and Culter. The TRC also received testimony from Janice Houston, Utah Foundation and Zach Frankel, Utah Rivers Council.

2. Testimony of Christine Finlinson, Central Utah Water Conservancy District, October 25, 2002.

3. Source: Unpublished data provided by Janice Houston, Research Analyst, Utah Foundation.

4. Source: Unpublished data provided by Janice Houston, Research Analyst, Utah Foundation.

5. These five districts are: Central Utah Water Conservancy District, Jordan Valley Water Conservancy District, Metropolitan Water District of Salt Lake City and Sandy, Washington County Water Conservancy District, and Weber Basin Water Conservancy District. The fiscal year for the Washington County Water Conservancy district ended on December 31, 2001 and for all other districts the fiscal year ended on June 30, 2001.